

IT 96-15

Tax Type: INCOME TAX

Issue: Penalty Under 1002(d) - Failure To File/Pay Withholding

STATE OF ILLINOIS
DEPARTMENT OF REVENUE
ADMINISTRATIVE HEARINGS DIVISION
CHICAGO, ILLINOIS

THE DEPARTMENT OF REVENUE
OF THE STATE OF ILLINOIS

v.

TAXPAYER

Taxpayer

)
)
)
) SSN
)
) C. Ladewig
) Admin. Law Judge
)

RECOMMENDATION FOR DISPOSITION

Appearances: TAXPAYER, APPEARING PRO SE; MR. TOM JACOBSEN, SPECIAL ASSISTANT ATTORNEY GENERAL, FOR THE ILLINOIS DEPARTMENT OF REVENUE.

Synopsis:

THIS MATTER COMES ON FOR HEARING PURSUANT TO THE TAXPAYER'S TIMELY PROTEST OF NOTICE OF DEFICIENCY NO. XXXXXY ISSUED BY THE DEPARTMENT ON JUNE 24, 1994 FOR WITHHOLDING TAX LIABILITY. SUCH NOTICE OF DEFICIENCY WAS ISSUED TO TAXPAYER (HEREINAFTER "TAXPAYER" OR THE "TAXPAYER") AS A RESPONSIBLE OFFICER OF CORPORATION PURSUANT TO SECTION 1002(D) OF THE ILLINOIS INCOME TAX ACT.

THE ISSUES TO BE RESOLVED ARE 1) WHETHER THE TAXPAYER WAS A RESPONSIBLE OFFICER OF CORPORATION AND THEREBY REQUIRED TO COLLECT, TRUTHFULLY ACCOUNT FOR AND PAY OVER THE TAX IMPOSED BY ARTICLE 7 OF THE ILLINOIS INCOME TAX ACT AND 2) WHETHER THE TAXPAYER WILLFULLY FAILED TO COLLECT, TRUTHFULLY ACCOUNT FOR AND PAY OVER SUCH TAXES FOR THE THIRD QUARTER OF 1989 THROUGH THE FOURTH QUARTER OF 1991 (HEREINAFTER "TAX PERIOD").

A HEARING WAS HELD ON MARCH 14, 1995. UPON CONSIDERATION OF ALL THE EVIDENCE, IT IS RECOMMENDED THAT THIS MATTER BE RESOLVED IN FAVOR OF THE DEPARTMENT.

Findings of Fact:

1. THE DEPARTMENT'S PRIMA FACIE CASE WAS ESTABLISHED WITH THE INTRODUCTION INTO EVIDENCE OF THE NOTICE OF DEFICIENCY NO. XXXXXY DATED JUNE 24, 1994. DEPT. EX. NO. 3. THIS NOTICE OF DEFICIENCY PROPOSED A TAX LIABILITY FOR FAILURE TO PAY OVER TO THE STATE OF ILLINOIS INCOME TAXES WITHHELD FROM EMPLOYEES OF CORPORATION FOR THE THIRD QUARTER OF 1989 THROUGH THE FOURTH QUARTER OF 1991. DEPT. EX. NO. 3.

2. TAXPAYER WAS THE PRESIDENT OF CORPORATION DURING THE TAX PERIOD AND HELD THE TITLE OF VARIOUS OTHER OFFICES INCLUDING DIRECTOR FROM 1984 THROUGH THE COMPANY'S OFFICIAL DISSOLUTION IN 1993. TAXPAYER WAS ALSO A SHAREHOLDER THROUGHOUT THE SAME PERIOD OF TIME. TR. P. 47.

3. TAXPAYER WAS A SIGNATORY ON THE BANK ACCOUNTS AT XXXXX AND XXXXX. TR. P. 48. THESE ACCOUNTS WERE ACTIVE AT VARIOUS TIMES THROUGHOUT 1989, 1990 AND 1991. TR. PP. 48-49.

4. CORPORATION IS THE SAME LEGAL ENTITY AS CORPORATION. TR. P. 49. MR. TAXPAYER VERIFIED HIS SIGNATURE ON COPIES OF CHECKS FOR THE CORPORATION. DEPT. EX. NO. 6; TR. P. 49.

5. TAXPAYER WAS AWARE OF THE BALANCE IN THE ACCOUNTS FOR CORPORATION, HAD CONTROL OVER DISBURSEMENTS AND DETERMINED WHAT HAD TO BE PAID AND WHAT IN TURN WAS NOT PAID. TR. P. 50.

6. TAXPAYER BECAME AWARE THAT WITHHOLDING TAXES WERE OWED TO THE STATE OF ILLINOIS IN THE LATTER PART OF 1989. TR. P. 51.

7. TAXPAYER KEPT TRACK OF THE DEPOSITS TO THE BANK ACCOUNTS, SIGNED CHECKS AND ASSUMED THE CONTROLLER'S, CONTROLLER', RESPONSIBILITIES AFTER CONTROLLER LEFT IN DECEMBER 1990. TR. PP. 8, 52.

Conclusions of Law:

SECTION 1002(D) OF THE ILLINOIS INCOME TAX ACT IMPOSES A PENALTY ON:

ANY PERSON REQUIRED TO COLLECT, TRUTHFULLY ACCOUNT FOR, AND PAY OVER THE TAX IMPOSED BY THIS ACT WHO WILLFULLY FAILS TO COLLECT SUCH TAX OR TRUTHFULLY ACCOUNT FOR AND PAY OVER SUCH TAX OR WILLFULLY ATTEMPTS IN ANY MANNER TO EVADE OR DEFEAT THE TAX OR THE PAYMENT THEREOF, SHALL, IN ADDITION TO OTHER PENALTIES PROVIDED BY LAW, BE

LIABLE TO A PENALTY EQUAL TO THE TOTAL AMOUNT OF THE TAX EVADED, OR NOT COLLECTED, OR NOT ACCOUNTED FOR AND PAID OVER... .

35 ILCS 5/1002(D).

35 ILCS 5/1002(D) IS MODELED AFTER SECTION 6672 OF THE INTERNAL REVENUE CODE, WHICH IMPOSES LIABILITY UPON THOSE INDIVIDUAL PERSONS ACTUALLY RESPONSIBLE FOR AN EMPLOYER'S FAILURE TO WITHHOLD AND PAY OVER THE TAXES. ALLEN V. UNITED STATES, 547 F.SUPP. 357 (N.D. ILL. 1982).

IN DETERMINING WHETHER AN INDIVIDUAL IS A RESPONSIBLE PERSON THE COURTS HAVE INDICATED THAT THE FOCUS SHOULD BE ON WHETHER THAT PERSON HAS SIGNIFICANT CONTROL OVER THE BUSINESS AFFAIRS OF A CORPORATION, OR WHETHER THAT PERSON PARTICIPATES IN DECISIONS REGARDING WHAT BILLS SHOULD OR SHOULD NOT BE PAID AND WHEN. SEE, E.G. BLOOM V. UNITED STATES, 272 F.2D 215 (9TH CIR. 1959). RESPONSIBILITY FOR EMPLOYMENT TAXES IS A MATTER OF STATUS, DUTY, AND AUTHORITY, NOT MERELY A MATTER OF KNOWLEDGE CONCERNING THE EXISTENCE OF A CORPORATE TAX LIABILITY. MAZO V. UNITED STATES, 591 F.2D. 1151 (5TH CIR. 1979).

IN MONDAY V. UNITED STATES, 421 F.2D 1210, 1214-1215 (7TH CIR. 1970), CERT. DEN. 400 U.S. 821 (1970), THE COURT STATED THAT A RESPONSIBLE PERSON MAY BE AN OFFICIAL "CHARGED WITH GENERAL CONTROL OVER CORPORATE BUSINESS AFFAIRS WHO PARTICIPATES IN DECISIONS CONCERNING PAYMENT OF CREDITORS AND DISBURSAL OF FUNDS".

THE COURT IN SILBERBERG V. UNITED STATES, 524 F. SUPP. 744, 747 (E.D. N.Y. 1981), OUTLINED FIVE FACTORS WHICH GIVE GUIDANCE IN DETERMINING WHETHER AN INDIVIDUAL IS A RESPONSIBLE PERSON UNDER THE ACT: (1) THE CORPORATE IDENTITY OF THE INDIVIDUAL (WHETHER SUCH PERSON IS AN OFFICER, EMPLOYEE, DIRECTORS OR SHAREHOLDER), (2) HIS/HER DUTIES AS OUTLINED IN CORPORATE BY-LAWS, (3) THE EXTENT TO WHICH THE INDIVIDUAL IS AUTHORIZED TO SIGN CHECKS AND DISBURSE FUNDS, (4) WHETHER THE INDIVIDUAL HAS CONTROL OVER THE FINANCIAL AFFAIRS OF THE CORPORATION AND (5) WHETHER THAT INDIVIDUAL CAN HIRE AND FIRE EMPLOYEES. TAXPAYER TESTIFIED THAT HE WAS PRESIDENT, DIRECTOR AND A SHAREHOLDER DURING THE PERIOD WITHHOLDING TAXES WENT UNPAID. TR. P. 47. TAXPAYER HAD SIGNATORY AUTHORITY OVER THE COMPANY'S BANK ACCOUNTS FROM 1989 THROUGH 1991. ADDITIONALLY, TAXPAYER TESTIFIED THAT ALTHOUGH DISBURSEMENTS WERE NOT UNDER HIS SOLE CONTROL, HE WOULD MOST OF THE TIME HAVE KNOWN WHAT WAS BEING DISBURSED, WHAT THE EXPENSES WERE AND WHAT WAS BEING PAID AND NOT BEING PAID. TR. P. 50. SUCH CONTROL OVER FINANCIAL

MATTERS IS INDICIA OF RESPONSIBILITY UNDER THE STATUTE. THE FACT THAT OTHER OFFICERS MAY HAVE HAD CLOSER CONTROL DOES NOT EXONERATE MR. TAXPAYER FROM LIABILITY. SEE, GEPHART V. UNITED STATES, 818 F.2D 469 (6TH CIR. 1987)

TAXPAYER TESTIFIED THAT AFTER THE CONTROLLER, CONTROLLER, DEPARTURE IN DECEMBER 1990, HE ASSUMED EVEN MORE RESPONSIBILITY IN THAT HE WAS SIGNING CHECKS, KEEPING TRACK OF THE DEPOSITS TO THE BANK ACCOUNTS AND HANDLING OTHER DAY TO DAY SUPERVISORY DUTIES. TR. P. 52. CONTROLLER TESTIFIED THAT EVEN BEFORE HIS DEPARTURE HE KEPT MR. TAXPAYER APPRISED OF THE COMPANY'S FINANCIAL SITUATION, AT TIMES, ALMOST DAILY. TR. P. 10.

THE FACT THAT TAXPAYER DID NOT DAILY SUPERVISE PAYROLL DISBURSEMENTS BEFORE CONTROLLER' DEPARTURE DOES NOT PRECLUDE FINDING HIM A RESPONSIBLE PERSON. SEE, COOPERMAN V. UNITED STATES, 78-2 USTC PAR. 9578 (E.D. N.Y. 1978). (THE COURT FOCUSED ON THE QUALITY OF THE CONTROL EXERCISED RATHER THAN SIMPLY ITS FREQUENCY.)

IN THE PRESENT CASE THE TAXPAYER WAS A PERSON WHO COULD HAVE SEEN TO IT THAT THE WITHHELD INCOME TAXES WERE PAID TO THE STATE OF ILLINOIS. TAXPAYER WAS THE PRESIDENT OF CORPORATION DURING THE PERIOD AT ISSUE AND TESTIFIED AT HEARING THAT HE HAD AUTHORITY TO DETERMINE WHICH CREDITORS WERE PAID AND WHICH WERE NOT. TESTIMONY OF BOTH MR. TAXPAYER AND CONTROLLER INDICATES THAT CREDITORS SUCH AS XXXXX WERE BEING PAID DURING THE TIME PERIOD IN WHICH WITHHOLDING TAXES WERE OWED TO THE STATE OF ILLINOIS. TR. PP. 10, 51, 53.

UPON FINDING TAXPAYER A RESPONSIBLE PERSON, IT MUST ALSO BE DETERMINED WHETHER AS SUCH HE WILLFULLY FAILED TO REMIT THE WITHHOLDING TAXES TO THE DEPARTMENT. WILLFULNESS IN REGARDS TO SECTION 1002(D) IS NOT MERELY LIMITED TO "INTENTIONAL, KNOWING AND VOLUNTARY ACTS". YOUNG V. IRS, 85-1 USTC PAR. 87521. WILLFUL AS APPLIED IN SECTION 6672, AND HENCE 1002(D), "ENCOMPASSES VOLUNTARY OR INTENTIONAL ACTS, OR ACTIONS EXHIBITING A RECKLESS DISREGARD OF A KNOWN OR A OBVIOUS RISK THAT TAX MONIES HAVE NOT BEEN REMITTED TO THE TAXING ENTITY". ID.

COURTS HAVE INDICATED THAT THE DETERMINATION OF WHETHER AN EMPLOYEE KNOWINGLY, VOLUNTARILY AND INTENTIONALLY FAILS TO REMIT SUCH TAX IS "AN ISSUE OF FACT TO BE DETERMINED BY THE TRIER OF FACT ON THE BASIS OF THE CIRCUMSTANCES AND EVIDENCE ADDUCED IN THE PARTICULAR CASE." DEPARTMENT OF REVENUE V. BUBLICK, 68 ILL.2D 568, 577 (1977).¹

¹. The Illinois Supreme Court in Department of Revenue v. Heartland Investments, 106 Ill.2d 19, 29 (1985), accepted that cases arising under section 6672 of the IRC provided guidance in determining the meaning of the "willful failure" requirement of Chapter 120 par. 452 1/2 (13 1/2). See, e.g. Carl E. Branson v. The Department of Revenue, 168 Ill.2d 247 (1995). The court was addressing

IN THIS CASE, TAXPAYER CONTENDS THAT FAILURE TO PAY THE DEPARTMENT OF REVENUE WAS NOT WILLFUL BECAUSE IT WAS NOT A CONSCIOUS DECISION, RATHER IT HAPPENED AS A RESULT OF A DECISION TO PAY OTHER CREDITORS, SUCH AS UTILITIES OR MAJOR CREDITORS. TR. P. 53.

CASE LAW INDICATES THAT WILLFULNESS "IS PRESENT IF THE RESPONSIBLE PERSON HAD KNOWLEDGE OF THE TAX DELINQUENCY AND KNOWINGLY FAILED TO RECTIFY IT WHEN THERE WERE AVAILABLE FUNDS TO PAY THE GOVERNMENT". GEPHART V. UNITED STATES, SUPRA, AT 475.

TESTIMONY INDICATES THAT TAXPAYER BECAME AWARE THAT SUCH TAXES WERE DUE THE STATE IN THE LATTER PART OF 1989. TR. P. 51. HE INDICATED THAT HE KEPT TRACK OF SUCH TAX DUE IN ORDER TO SETTLE THE ACCOUNT WHEN THE COMPANY RECEIVED ADEQUATE FUNDING, WHICH, OF COURSE, NEVER HAPPENED. TR. P. 51. TAXPAYER ADMITS PREFERENCE TO CREDITORS SUCH AS BANKS, UTILITY COMPANIES AND MAJOR SUPPLIERS SUCH AS XXXXX WAS GIVEN DURING THE THIRD QUARTER OF 1989 UNTIL THE END OF 1991, THE TIME PERIOD THAT WITHHOLDING TAXES WERE DUE THE STATE OF ILLINOIS. TR. PP. 44, 53. COURTS HAVE FOUND THAT AN INTENT TO DEFRAUD THE GOVERNMENT IS NOT NECESSARY. RATHER, MERELY "KNOWINGLY USING AVAILABLE FUNDS TO PREFER OTHER CREDITORS OVER THE GOVERNMENT" IS ENOUGH TO CONSTITUTE WILLFULNESS. MONDAY V. UNITED STATES, SUPRA, AT 1216; DEPARTMENT OF REVENUE V. HEARTLAND INVESTMENTS, SUPRA.

LASTLY, WITH REGARD TO TAXPAYER'S ATTEMPT TO INTRODUCE EVIDENCE TO REVISE THE AMOUNT STATED ON THE NOTICE OF DEFICIENCY, SECTION 904(B) PROVIDES GUIDANCE. SECTION 904(B) READS IN PART:

IF THE TAXPAYER FAILS TO FILE A TAX RETURN, THE DEPARTMENT SHALL DETERMINE THE AMOUNT OF TAX DUE ACCORDING TO ITS BEST JUDGMENT AND INFORMATION, WHICH AMOUNT SO FIXED BY THE DEPARTMENT SHALL BE PRIMA FACIE CORRECT AND SHALL BE PRIMA FACIE EVIDENCE OF THE CORRECTNESS OF THE AMOUNT OF TAX DUE.

35 ILCS 5/904(B).

TAXPAYER HAS THE BURDEN TO PRODUCE COMPETENT EVIDENCE TO OVERCOME THE DEPARTMENT'S PRIMA FACIE CASE. COPILEVITZ V. DEPARTMENT OF REVENUE, 41 ILL.2D 154, 156 (1968). IF THE EVIDENCE PUT FORTH BY THE TAXPAYER "IS NOT SO INCONSISTENT OR IMPROBABLE IN ITSELF AS TO BE UNWORTHY OF BELIEF, THE BURDEN THEN SHIFTS TO THE DEPARTMENT". FILLICHIO V. IDOR, 15 ILL.2D 327, 333 (1958).

the Retailers' Occupation Tax Act in the Heartland decision, however, not only are the underlying policies of the ROT section and section 1002(d) similar but the language of the two section encompasses both responsibility and willfulness.

IN THE PRESENT CASE, THE TAXPAYER PRODUCED LISTS OF EMPLOYEES WHO HE CLAIMS WERE NEVER PAID. ACCORDING TO TAXPAYER'S TESTIMONY AT HEARING, THE FIGURES PROVIDED BY THE PAYROLL SERVICE ARE INACCURATE BECAUSE MANY OF THE CHECKS ISSUED TO EMPLOYEES WERE NEVER CASHED. TR. PP. 56, 57. HOWEVER, THE TAXPAYER FAILED TO PROVIDE COMPETENT EVIDENCE WHICH PROVED SUCH CHECKS NEVER CLEARED THROUGH THE CORPORATION'S PAYROLL ACCOUNT. FURTHERMORE, THE FEDERAL WITHHOLDING RETURNS PRODUCED BY TAXPAYER AT HEARING CANNOT BE GIVEN ANY CREDIBILITY AS THERE IS NO EVIDENCE THAT THESE RETURNS WERE FILED.

AFTER REVIEWING ALL THE EVIDENCE SUBMITTED AT HEARING, IT WAS DETERMINED THAT THE TAXPAYER DID NOT PROVIDE SUFFICIENT COMPETENT EVIDENCE TO OVERCOME THE DEPARTMENT'S PRIMA FACIE CASE.

WHEREFORE, FOR THE REASONS STATED ABOVE, IT IS MY RECOMMENDATION THE NOTICE OF DEFICIENCY BE FINALIZED AS ISSUED.

CHRISTINE E. LADEWIG

ADMINISTRATIVE LAW JUDGE